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RUEHDK/AMEMBASSY DAKAR 2638
RUEHKM/AMEMBASSY KAMPALA 3056
RUEHNR/AMEMBASSY NAIROBI 5499
RUEAIIA/CIA WASHDC
RUEHGV/USMISSION GENEVA 2184
RHEHAAA/NSC WASHDC
RHMFISS/JOINT STAFF WASHDC
RUEHC/DEPT OF LABOR WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RHEFDIA/DIA WASHDC
RUCPDOC/DEPT OF COMMERCE WASHDC
RUZEJAA/JAC MOLESWORTH RAF MOLESWORTH UK
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UNCLAS SECTION 01 OF 05 HARARE 000499

SENSITIVE
SIPDIS

AF/S FOR B. WALCH
AF/EPS FOR ANN BREITER
NSC FOR SENIOR AFRICA DIRECTOR
STATE PASS TO USAID FOR L.DOBBINS AND J. HARMON
TREASURY FOR D. PETERS
COMMERCE FOR ROBERT TELCHIN
ADDIS ABABA FOR USAU
ADDIS ABABA FOR ACSS

E.O. 12958: N/A
TAGS: EMIN ETRD ECON PGOV ZI
SUBJECT: GOLD'S POTENTIAL TO CONTRIBUTE TO ZIMBABWE'S
ECONOMIC RECOVERY

SUMMARY

¶1. (SBU) Zimbabwe is in dire need of substantial foreign currency inflows. Looking ahead, the country's once significant gold mining industry is a potential source of foreign exchange earnings, provided the problems of access to capital, power shortages, and protection of property rights are addressed. The recent liberalization of gold policy has helped revive the industry, but producers still face serious constraints. Moreover, they are calling for consistent implementation of more market-friendly policies that will attract the foreign investment needed to increase exploration and production. Foremost, the Indigenization and Economic Empowerment Act and the proposed amendment to the Mines and Minerals Acts require substantive review to make them more investor-friendly. END SUMMARY.

Gold Offers Hope

¶2. (SBU) Zimbabwe's dire lack of foreign exchange is threatening the survival of the inclusive government. The collapse in value of the local currency after the explosive growth in money supply in 2008 forced the GOZ to abandon the Zimbabwe dollar as a medium of exchange. No longer able to print local currency with abandon to buy hard currency, Zimbabwe must now quickly develop alternative sources of foreign exchange. As the international donor community remains on the side line with economic assistance until the inclusive government introduces bolder political and economic

reforms, the resuscitation of Zimbabwe's gold mining industry offers hope as a potential source of foreign exchange in the near term.

Output Crashed under Bad Policies

¶3. (SBU) According to David Matyanga, chief economist of the Chamber of Mines of Zimbabwe, Zimbabwe's gold production fell by 49 percent from 7.018 MT in 2007 to 3.58 MT in 2008. Matyanga attributed the decline from the most recent production peak of 27 MT in 1996 to the overvalued Zimbabwe dollar and a government policy of paying producers far less than the world gold price. Gold producers whom we interviewed identified further constraints on output from both large- and small-scale miners.

Arrears to Producers

¶4. (SBU) Paul Markham, Technical Director and board member of one of Zimbabwe's major gold producers, Rio Tinto Zimbabwe Limited, told economic specialist that an acute lack of working capital had adversely affected production in 2008. He attributed the shortfall to the Reserve Bank of Zimbabwe,s (RBZ) US$30 million in arrears to producers for gold delivered to Fidelity Printers and Refiners (Private) Limited as of end-2008. Caxton Mangezi, General Manager of
QLimited as of end-2008. Caxton Mangezi, General Manager of

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developed countries, such as Australia, as a result of the global financial crisis. Mangezi added that his large company had not lost a significant number of managerial staff, and agreed with Markham that Zimbabwean geologists and surveyors had begun to return from abroad.

New Gold Marketing Rules Roundly Praised

¶8. (SBU) The industry roundly applauded as progressive the liberalization of gold marketing introduced by the RBZ in its January 2009 Monetary Policy Statement. Markam told us that the policy shift and the subsequent removal of the 7.5 percent foreign currency surrender requirements per Budget Review Statement of March 2009 made gold production profitable once again. (NOTE: Previously gold producers had to sell 7.5 percent of their foreign exchange receipts to the RBZ at a highly overvalued exchange rate. END NOTE.) Matyanga told us that most large-scale gold producers now send their gold to the RBZ's Fidelity Printers and Refiners through the Chamber of Mines. Fidelity does the assaying, consolidates the output, ships it to the Rand Refinery in South Africa, and credits each producer's account with the sales revenue. Mangezi felt that the new marketing and payment arrangements would stimulate gold output, especially given the current high gold price. Gura of Metallon, on the other hand, saw the liberalization of gold marketing as a temporary measure brought about by Zimbabwe having failed to produce 10 MT/year which caused Fidelity to lose its gold license at the London Bullion Marketing Association. He believed that once the industry reached the 10 MT threshold again, Fidelity would seize back the independent marketing of gold.

¶9. (SBU) Chimbodza told us that the changes to gold marketing were equally positive for small-scale gold producers who

could now get the world price on delivery of their product. He added that the policy shift would encourage small producers to sell gold through official channels. (NOTE: The small-scale sector produced as much as 50 percent of Zimbabwe's gold output as recently as in 1999. END NOTE.) Matyanga was less optimistic about the resurgence of small-scale gold producers in the short term. The sector needed significant capital investment to enable blasting, setting up rock supports, and ventilation since the easily-mined gold was nearly depleted. In his view, small-scale producers were unlikely to contribute more than 30 percent in the short term.

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Suspension of Royalty Payments a Boost to the Sector
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¶10. (SBU) The RBZ suspended payment of 3 percent royalty fee in 2004 in a bid to boost gold production. Gura anticipates re-introduction of the royalty following the removal of the 7.5 percent foreign exchange surrender requirement to the RBZ. Minister of Finance Tendai Biti has told producers that they will have to pay royalties now that they may retain 100 percent of their sales proceeds, although he has not indicated when this would occur. Victor Gapare, President of the Chamber of Mines and himself a gold miner,

pointed out that royalties should be less than in Tanzania, South Africa, Mali or Ghana, as Zimbabwe's yield of gold per ton of rock is less than half the rate in those countries. For now, at least, the absence of royalties is another incentive to producers to increase output.

More Needs to be Done

¶11. (SBU) Markham made the point that gold producers did not want aid or subsidies, rather an economic environment characterized by consistently implemented market-friendly policies. He said that while the Short Term Economic Recovery Program (STERP) launched by Minister Biti contained the right policies, they may prove to be unpopular and consequently not consistently implemented by government. Gura and other gold producers told us they would like to see the positive changes to gold policy set forth in the January 2009 Monetary Policy Statement reflected in an amendment to the Gold Trade Act and no longer subject to the whim of the Reserve Bank. In addition, Gura questioned the onerous requirement for taxes to be paid on a quarterly basis, as the currency--the U.S. dollar--was no longer losing value overnight. The requirement was a further drain on working capital at a time when it was needed most.

Current Output

¶12. (SBU) Matyanga expects gold production to roughly double to 6-7 MT in 2009. Markham told us in April 2009 that monthly production was 140 kg, with Rio Zim's Renco Mine accounting for almost half of it. In his view, the prevailing high gold price underpinned by tight supply could lift output substantially if the sector were able to recapitalize and if workers' wage demands were realistic. The outgoing President of the Chamber of Mines, David Murangari, went further to state that the sector would welcome flexibility in the labor market. He called for wages to be linked to productivity and for greater freedom for employers to retrench workers during lean times. Labor unions are asking for wages of US$454/month, which the economy cannot sustain. Most mines pay workers about US$100/month plus free housing, school fees for workers' children, medical insurance, etc.

COMMENT

¶13. (SBU) Zimbabwe is desperate for foreign exchange. Given the country's considerable gold resources, its gold mining tradition, and gold's firm and stable price, establishing policies that attract capital and that promote gold mining could generate considerable foreign exchange inflows in the next year. The restoration of the rule of law and respect for property rights would be a catalyst for investment and renewed exploration in this important sector. In this
Qrenewed exploration in this important sector. In this
regard, the Indigenization and Economic Empowerment Act requires substantive review, along with the proposed amendment to the Mines and Minerals Act. They need to be

more foreign-investor friendly as indigenous Zimbabweans clearly are not in a position to raise sufficient funds on the local market to revive and expand this important and capital-intensive subsector of the mining industry. END COMMENT.

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